

Valuing Professional Practices

Professional practices are businesses. As with any other business they need to make profits to survive.

The same principles and process should be applied in valuing them as we do with other businesses.

They share the problems of many service businesses – they can be highly profitable but have relatively low tangible assets. Professional practices generally have additional and particular problems. Requirements for professional qualifications and designations impose a major barrier to entry and limit the pool of buyers. Much of the value will be in intangibles – reputation, assembled workforce, customer databases, etc. – which do not appear on the Statement of Financial Position but are the real value drivers. Also, there may be a very high level of personal goodwill deriving from the practice owner's skills, experience, and relationships. This personal goodwill may be largely non-transferable.

As with many businesses professional practices will have different values for different buyers. Existing practices looking to grow through acquisition may extract more value through synergies or economies of scale.

Factors that will attract the premium purchaser include an excellent profits history, higher fee structure, attractive location, community reputation, and specialisations that provide a point of difference.

The basic valuation process is the same as for other businesses – full information, internal and external analysis and risk assessment, normalisation of financial accounts, consideration of the various appraisal approaches, arriving at an opinion of value and applying a sanity test. While many professions have rules of thumb which provide value indications these are dangerous to use in isolation as clearly demonstrated in Bizstats™ statistics on the sale of accountancy practices.

With the sale of professional practices the terms and conditions can be extremely important. A suitable non-compete clause, assistance period and payment terms can significantly affect the price. An earn-out provision with client retention or performance guarantees are often the norm.

With practices there may be both practice goodwill and personal goodwill. It is generally accepted that goodwill must be transferable and not personal to have commercial value. But some procedures can achieve a partial transfer of personal goodwill from an experienced practitioner – letters of introduction, long-term transition periods and employment contracts with key personnel.

Valuing and selling professional practices offers interesting challenges that we do not encounter with more conventional businesses.

For clear, accurate and affordable independent business valuations please contact us.

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